No. 211.

Brief of Wheeler for Respondent

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Supreme Court of the United States.

OCTOBER TERM, 1897.

C. H. BOSWORTH, RECEIVER OF THE CHICAGO, PEORIA & ST. LOUIS RAILWAY, *Appellant*,

vs.

TERMINAL RAILROAD ASSOCIATION OF ST. LOUIS, INTERVENING PETITIONER, *Appellee*.

BRIEF AND ARGUMENT OF APPELLEE IN OPPOSITION TO THE APPLICATION FOR WRIT OF CERTIORARI.

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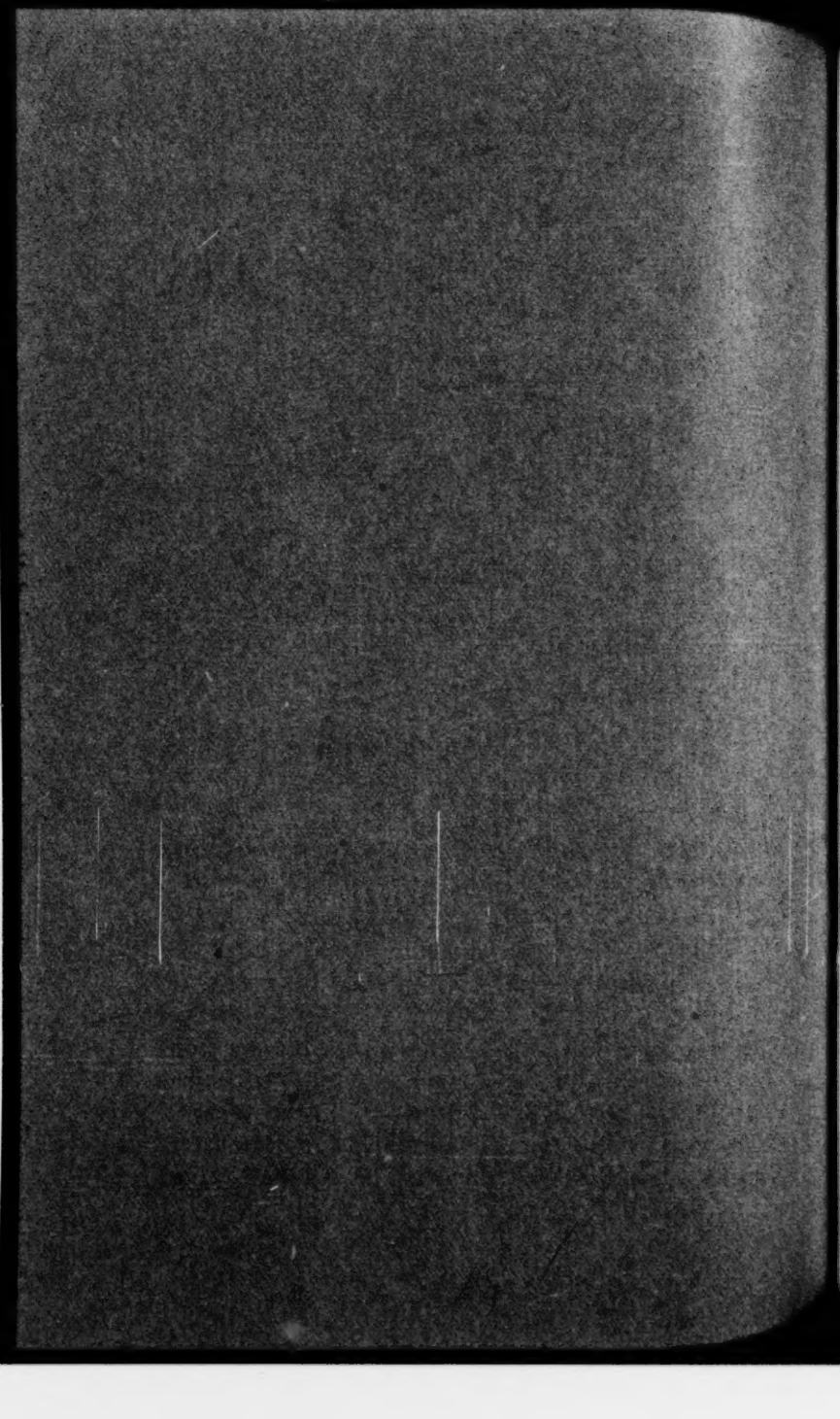

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The application for writ of certiorari is based upon the claim that the decision of the Circuit Court of Appeals in this cause is at variance with the decisions of the Circuit Court of Appeals of the Fourth and Sixth Circuits, and with the decisions of this court.

The precise question adjudicated by the Court of Appeals of the Seventh Circuit can be best determined

by an examination of the statement of the case made by that court and its decision thereon, which are as follows:

IN THE

UNITED STATES CIRCUIT COURT OF APPEALS.

FOR THE SEVENTH CIRCUIT.

No. 367.—October Term, 1896, May Session, 1897.

C. H. Bosworth, Receiver of the Chicago, Peoria and St. Louis Railway Company,
Appellant,
vs.
Terminal Railroad Association of St. Louis,
Intervening Petitioner.

Appeal from the Circuit Court of the United States, for the Southern District of Illinois.

Before WOODS, JENKINS and SHOWALTER, Circuit Judges.

In a suit brought by the Mercantile Trust Company on the 21st day of September, A. D. 1893, to foreclose a mortgage upon the Chicago, Peoria and St. Louis Railway, the court appointed a receiver with the authority usually conferred upon receivers in the charge and operation of railways and in the general administration of the estate, and required the receiver to pay (1) all past due taxes, (2) all current operating expenses, (3) all past due wages, (4) "all claims for materials and supplies which have been incurred in the operation and maintenance of said property during the six months last past, and all ticket, trackage and traffic balances due from said railroad;" to this last item the Mercantile Trust Company objected, which objection the court overruled.

On the 27th day of May, 1895, the Terminal Railroad Association of St. Louis, the appellee, filed its intervening petition asserting a claim against the railway company amounting to $8,162.11 for switching, engine and car repairs, etc., done within six months prior to the date of the order appointing a receiver and asking for the allowance of the claim as a preferential claim under the order of the court appointing the receiver. An answer was filed to this petition by the receiver asserting that the facts stated might be true for anything known to the contrary, but, being stranger to the matters, he demanded strict proof, and denying that the petitioner was entitled to the relief demanded. The intervening petition under a general order of reference went to the master, whose report was to the effect that the claim was a just one and that the amount is a lien upon the property of the railway company prior and superior to the claims of the mortgage bondholders under the order appointing the receiver, and that it should be paid out of the surplus income or from a sale of the property of the railway company. To this report the receiver filed exceptions, not impugning the finding of the master that the claim was a just one against the company, but to the finding that the claim should be paid from the surplus income or from a sale of the property of the railway company, "whereas," the exception proceeds, "the said master should have found that the aforesaid amount is due the said petitioner but is not a lien upon the property of the railway company prior or superior to the lien of the mortgage bondholders." Upon hearing the court, on July 30, 1896, overruled the exceptions and entered a decree allowing the claim at the amount stated; and declaring that it was a claim of the character embraced in the order appointing the receiver to be paid as a preferred claim and directing that the receiver pay to the intervener the amount of the claim "out of the

income of said receivership, if any such income is in his hands, and in case he has not the funds in hand for this purpose it is ordered, adjudged and decreed that the same be paid out of the proceeds of the sale of the mortgaged premises in preference to the mortgage debt, and until paid the same is hereby declared a lien upon the said mortgaged estate superior to the lien of the mortgage herein." To this decree the receiver assigned error in substance to the effect that the court erred in adjudging that the claim of the intervening petitioner was entitled to priority to the mortgage debt. The receiver thereupon prayed an appeal which was allowed.

JENKINS, Circuit Judge, delivered the opinion of the court:

The contention of the receiver is thus stated in the brief of his counsel: "The question thus presented to this court for determination is one as to the displacement of vested contract liens by unsecured creditors. There is no controversy as to the labor having been performed or the materials furnished within the six months next prior to the appointment of the receiver of the insolvent corporation, nor as to the value of the same. The only controversy is as to whether or not the appellee is entitled on its petition and proof made thereunder to have the vested lien of the mortgagee displaced to the extent of his claim." He insists that the provision in the decree appointing a receiver providing for the payment of certain claims as preferential created no vested right, and that within our ruling in *Mather Humane Stock Transportation Company vs. Anderson*, 46 U. S. App. 138, the decree in that regard was interlocutory and is not controlling of the subsequent action of the court; and that within the doctrine declared in *Turner vs. The Indianapolis, Bloomington and Western Railway Company*, 8 Bis-

sell, 315; *Fosdick vs. Schall*, 99 U. S. 235; *Union Trust Company vs. Souther*, 107 U. S. 591; *Burnham vs. Bowen*, 111 U. S. 776; *Union Trust Company vs. Illinois Midland Railway Company*, 117 U. S. 432; *Wood vs. Guarantee Trust and Safe Deposit Company*, 128 U. S. 416; *Kneeland vs. American Loan and Trust Company*, 138 U. S. 89; *Thomas vs. Western Car Company*, 149 U. S. 111; *Farmers' Loan and Trust Company vs. Green Bay, W. & St. P. Railway Company*, 45 F. R. 664, before a claim can be deemed to be preferential to the mortgage debt, there must be first established a diversion of income from the payment of operating expenses to the payment of interest and that, failing diversion, there can be no restoration. The broad ground is taken that a court of equity, assuming at the request of a trustee the operation of a railway, has not the right to provide for the payment, out of the income or the corpus of the road, of operating expenses incurred within a limited time prior to the suit, unless there has been diversion of income and then only to the extent of such diversion.

It is, however, objected by the appellee that with this question the receiver is not concerned and that, the justice of the debt being conceded, it is none of his affair that it is preferred by the decree to the mortgage debt. This contention, we think, must be sustained. While it is true that a receiver is the instrument of the court for the conservation of the estate which the court has taken into its possession for administration, it is also true that in a sense he represents all parties in interest. His duty is to defend the estate against all claims which he deems to be unjust; his duty is to conserve the estate as a whole for its distribution by the court among those who shall be adjudged to be entitled; he represents the estate, with right to sue to recover demands due to it; with right to defend it

against claims asserted. In this respect we concur with the Circuit Court of Appeals for the Fourth Circuit that this duty carries with it the right and the duty, in case of doubtful claim, to take the judgment of the court of last resort. *Thom. vs. Pittard*, 8 U. S. App. 597. This right and duty should, however, be limited in its exercise to those cases in which the estate, as a whole, is interested to enforce a right or to defend against a claim asserted. In respect to many matters, the receiver has no right to appeal, while in respect to others, his right of appeal may not be gainsaid. Thus, he may rightfully appeal from a decree refusing him compensation, or disallowing his accounts, or establishing a claim against the estate, or denying a claim asserted for the estate. He has no right to appeal from a decree removing him from his position, for that is matter of discretion with the court appointing him, and he holds his position by the sufferance of the court; nor has he the right of appeal from a decree authorizing an issue of receivers' certificates, or directing a particular management of the trust property, or directing sale of the mortgaged property or confirming its sale, or directing the turning over of property in his hands; for he is neither the censor of the court nor interested in the event. Illustrations might be multiplied. The true line of demarcation, we think to be this: He has the right of appeal with respect to any claim asserted by or against the estate, for therein he is the representative of the entire estate; he has the right of appeal from any decree which affects his personal right, for therein he has an interest; but he has not the right of appeal from a decree declaring the respective equities of parties to the suit. He should therein be indifferent and not a partisan. His duty is to all parties in common. He should not become the advocate of one against another. *Security Trust Company vs. Sullivan*, 45 U. S. App. 601, 603.

The record here is not complete. There has been brought to this court only so much of the record as is thought to bear upon the particular question which the receiver desired to present. It was, however, conceded at the argument that prior to the decree appealed from the railway had been sold under decree of sale and had passed out of the possession of the receiver and into the possession of the purchaser, and that the receiver had not in hand moneys with which to pay the debt adjudged. That this debt was a just claim against the estate is not doubted and is conceded. No objection is taken to its allowance, nor is it questioned that under the decree appointing the receiver it was a proper claim to be paid in preference to the mortgage; but the receiver asserts that the decree allowing preferential claims was improvident, and that the mortgage had preference in payment, because there had been in fact no diversion of income to the payment of interest. Neither the trustee, nor the bondholders, nor the purchaser is here objecting. Who made the receiver the guardian of their interests in this regard? What duty is imposed upon him to assert the supposed right of one creditor over another in respect to a common fund; and this, whether the estate remains in his custody or has passed from his possession and control under decree and sale? By what right does he become the partisan advocate when his duty demands of him impartiality and indifference with respect to the division of this common fund? By what authority may he assert the rights of a purchaser? By what right does he undertake to prevent the enforcement of this claim against the purchased estate, presumably by the decree of sale charged as a lien upon it? He has no such right. He is in so doing an interloper obtruding himself in breach of his duty where he has no right and in a matter with which he is not concerned. To sanction such action is to encourage vexatious litigation at the expense of the estate which should be cast upon the

interested parties, and to hold out the temptation to a receiver and his counsel to swell the cost of administration by assuming litigation with which he has no right to interfere.

It was held in *Farlow vs. Kelley*, 131 U. S. Appendix, cci, that the allowance by a circuit court of an appeal taken by a receiver is equivalent to leave by the court to the receiver to take an appeal, and it is urged that since the appeal here was allowed by the Circuit Court according to usual practice, we are bound to entertain it and to determine the question which the receiver has presented. In some States it is held that no case may be appealed by a receiver without permission, notwithstanding parties may appeal as of right and without leave. The Supreme Court, in the case referred to, merely holds that if leave were essential it was granted by the usual allowance of an appeal; but it is nowhere held, and the doctrine cannot be sanctioned, that the allowance of an appeal can operate to clothe the receiver with an interest which he has not, or can impose upon an appelate court the duty of hearing and determining a moot question.

The appeal will be dismissed.

It clearly appears, from the examination of the opinion, that the Court of Appeals passed upon but one question. When appointing appellant receiver of the insolvent railway company the court made the usual order directing the payment of claims for labor and materials accruing within the six months next prior to the appointment of the receiver, thus giving preference to such claims over the lien of the mortgage debt. It was conceded that the appellee's claim was just and came within the terms of the order of the court. The claim was allowed by the master in chancery, exceptions to his findings overruled, and

an order entered by the Circuit Court directing the receiver to pay the claim. The receiver alone resisted the payment; none of the bondholders or other creditors objected. The receiver appealed to the Court of Appeals, and in that court appellee insisted that the receiver had no appealable interest in the controversy. The Court of Appeals sustained this contention. This was the one point decided by the Court of Appeals, and in passing upon this point the Court of Appeals said: "That this debt was a just claim against the estate is not doubted and is conceded. No objection is taken to its allowance, nor is it questioned that under the decree appointing the receiver it was a proper claim to be paid in preference to the mortgage, but the receiver asserts that the decree allowing preferential claims was improvident and that the mortgage had preference in payment because there had been, in fact, no diversion of income to the payment of interest. Neither the trustee, nor the bondholders, nor the purchaser is here objecting. Who made the receiver the guardian of their interest in this regard? What duty is imposed upon him to assert the supposed right of one creditor over another in respect to a common fund; and this, whether the estate remains in his custody or has passed from his possession and control under the decree of sale? By what right does he become the partisan advocate when his duty demands of him impartiality and indifference with respect to the division of this common fund? By what right does he undertake to prevent the enforcement of this claim against the purchased estate, presumably by the decree of sale charged as a lien upon it? He has

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Appellant will search in vain for a decision of any court, State or Federal, which is at variance with this ruling.

The case of *Thom vs. Pittard*, *supra*, was cited, commented upon, and the principle of law therein enunciated fully assented to in the opinion of the Court of Appeals in this cause. The principle laid down in *Felton vs. Ackerman* is in entire harmony with the opinion of the Court of Appeals in this cause and with the opinion in *Thom vs. Pittard;* that principle is elementary and is well stated by the Court of Appeals in its opinion in this cause, as follows: "While it is true that a receiver is the instrument of the court for the conservation of the estate which the court has taken into its possession for administration, it is also true that in a sense he represents all parties in interest. His duty is to defend the estate against all claims which he deems to be unjust; his duty is to conserve the estate as a whole for its distribution by the court among those who shall be adjudged to be entitled; he represents the estate with right to sue to recover demands due to it; with right to defend it against claims asserted." The court continues: "He has no right to appeal from a

decree removing him from his position, for that is matter of discretion with the court appointing him, and he holds his position by the sufferance of the court; nor has he the right of appeal from a decree authorizing the issue of receivers' certificates, or directing a particular management of the trust property, or directing a sale of the mortgaged property or confirming its sale, or directing the turning over of property in his hands; for he is neither the censor of the court nor interested in the event. Illustrations might be multiplied. The true line of demarcation we think to be this: He has the right of appeal with respect to any claim asserted by or against the estate, for therein he is the representative of the entire estate; he has the right of appeal from any decree that affects his personal right, for therein he has an interest; but he has not the right of appeal from a decree declaring the respective equities of parties to the suit. He should therein be indifferent and not a partisan. His duty is to all parties in common, he should not become the advocate of one against another. *Security Trust Company vs. Sullivan*, 45 U. S. App. 601, 603."

In his petition for the writ of certiorari in this case (p. 8), appellant says: "The meritorious question presented to said Court of Appeals, by said appeal, was as to the right to displace vested contract liens in favor of unsecured creditors in railroad foreclosures where there had been no diversion of income." The question thus stated by the appellant himself is manifestly one in which he has no concern; having no concern in this question at any stage of this cause, in the Circuit Court where the suit originated, or in the Cir-

cuit Court of Appeals to which the appeal was taken, he has no interest in the determination of this question by this court.

The decree of the Circuit Court, from which the receiver appealed to the Court of Appeals for the Seventh Circuit, was an order directing the receiver, as an officer of the court, to pay a certain amount of money out of the funds that were or might come into his hands as such officer. The receiver admitted that appellee's claim was justly due, but resisted its payment upon the one ground that such payment would "displace the vested contract lien of the mortgage bondholders." As such officer of the court, in physical possession of funds entrusted to him by that court, what interest has he in a controversy between rival claimants to a portion of that fund? As such officer of the court, how does it become any part of his duty to protect complainant in a foreclosure proceeding against the operation of the decree of the court? The decree did not in any manner or to any extent impair the fund of which the receiver was custodian. The decree was, in fact, nothing more or less than an order of distribution, and as between distributees created a preference in favor of one as against the other. What interest had the receiver in this preference? This preference was created in the first instance in the order appointing the receiver. Could the receiver, taking possession under that order, clothed with whatever power he may possess by virtue thereof, have objected to this provision of the order? If he had no right to object to this provision of the order, what right has he to object when instructed to act in pursuance of such order? In taking

his appeal from the Circuit Court the basis of the appeal was that the original order was improvident; that in making such order the court could not displace the vested contract right of the bondholder, and that, although the bondholder himself did not object, the receiver would object for him. In asking for the writ of certiorari in this cause, the receiver becomes, not only the censor of the court of which he was an officer, but a censor of the Circuit Court of Appeals for the Seventh Circuit, to which he asks the writ of certiorari in this cause to be directed.

It concerns him not that the order of the court appointing the receiver gave preference to appellee's claim over the debt of the bondholder. He has no right to "take sides" with the bondholder or with appellee. It was his duty to know that the claim was just and fair, and that it came within the purview of the order of the court. In putting appellee to the proof of these facts, he but did his duty; here his duty, so far as any objection to the payment of appellee's claim is concerned, ended. He forgets and disregards that duty when he attacks the propriety of the order of the court creating the preference, and when he asks that the cause may be transferred to this court for its determination of the propriety of that order. The Circuit Court, in taking possession of the property, at the request of the bondholders, saw fit to direct that claims for labor and supplies incurred within six months prior to the appointment should be paid. The only parties interested in this order are the parties who would eventually become entitled to the surplus income and proceeds of the sale of the property. None of these parties are

here objecting. The objections the receiver makes to the payment of appellee's claim go not to the justness of the claim, but to the propriety of the order made by the court in the first instance.

The receiver forgets that when the court took possession of the property of the insolvent railway company, it was for the purpose of doing that which the railway company could not or would not do, namely: paying the creditors of the railway company, unsecured as well as secured, in the order in which equity might determine the priorities. Nor does he now seem able to comprehend the fact that the question of *preference or priority as between creditors is one which concerns the creditors only.* The debt of the insolvent railway company to appellee, for material furnished and labor performed, within the period fixed by the court giving priority to such claims when properly presented and allowed, and conceded to be just, became a claim against the *estate of the insolvent railway company in the receiver's hands.* It matters not at whose instance, or what may be the nature or character of the legal procedure, whenever the estate of an insolvent comes in *custodia legis*, the party appointed by the Court of Chancery to take possession for that court, holds "for the benefit of whomsoever in the end it shall be found to concern, and in the meantime the court proceeds to determine the rights of the parties upon the same principle it would if no change of possession had taken place." *Fosdick vs. Schall*, 99 U. S. 235. It is, however, apparent that in construing this citation the receiver has inadvertently substituted the word "receiver" for the word "court"; for he seeks to make it

his duty to determine the rights of the parties, and having done this to direct the court to make the distribution in accordance with *his* findings.

The receiver apparently finds some difficulty in understanding the fact that the payment of a just debt allowed against the estate is not a diminution of the estate. The moment appellee's claim was allowed and conceded to be just, the appellee became, so far as the receiver is concerned, an absolute creditor of the estate, as much a creditor as the bondholder; and the payment of appellee's claim would be no more a diminution of the estate than would be the payment of the bondholder's claim—the question of priority between the two concerns these two alone. The difference between the *diminution of the estate*—loss by fire, accident, theft, or taking of part of the assets by some one not a just creditor—and the *distribution of the assets of the estate*, the receiver wholly fails to grasp. From his standpoint every payment he makes out of the assets of the estate—the payment of his own salary, the payment of the fees of his counsel, the payment for supplies used by him in the operation of the property —is a diminution of the assets of the estate, and should be strenuously opposed, and he would be doing only his duty in "carrying that resistance to the court of last resort."

The receiver admits that there is no defense to the claim as against the railway company, but resists its payment solely on the ground that such payment would displace the vested contract lien of the bondholders. And yet, he resents the charge that he has "become the partisan advocate, when his duty de-

mands of him impartiality and indifference with respect to the division of this common fund." (Opinion, *supra.*) It is difficult to conceive in what way he could make himself more distinctly, confessedly and avowedly the unsolicited champion of the interests of the uncomplaining mortgagee or purchaser under the foreclosure proceedings, nor how he could show a greater disregard of his duty to remain impartial as between the creditors contesting the right of priority.

Great stress is placed on the case of *McLeod vs. City of New Albany*, 66 Fed. Rep. 378. The decision in that case is in entire harmony with the decision rendered in this cause, and is within the unbroken line of decisions defining the receiver's duty. In the quotation given by the receiver from the *McLeod* case occurs this passage: "It was their duty to preserve the estate and to pay the taxes thereon. *If the taxes were illegally laid*, it was their duty, representing all the interests, to contest the payment." In that case, as in this, it was the duty of the receiver to see that the claim was *just.* The justness of the claim being conceded, the receiver's duty ended so far as resistance of payment of the claim was concerned. And so in every case cited by the receiver in support of his right to take the appeal, such right has been conceded only where the determination of the question involved might work a diminution or increase of the estate as a whole. The same is true of the citations from the text writers, *High* and *Beach.* For instance, in the citation from *High*, that author says, the receiver "has the same right to appeal from an adverse judgment for the recovery of funds pertaining to his receivership

as the party over whom he was appointed would have." And in the citation from *Beach*, it is said: "The receiver, as a party defendant to the action, has the same right to appeal from a judgment of the court affecting the interests of the estate represented by him that the *party or corporation to whom the estate originally belonged would have had* if the suit had been brought against them." In other words, these text writers hold this and only this, that the receiver can make for the party, whose property has been placed in his hands, the same defense the party himself could make. This principle has never been questioned, but it being admitted in this case that the railway company could make no defense to appellee's claim, it follows of necessity the receiver can make no defense. The failure on the part of the receiver to comprehend the difference between *diminution of the estate* and *distribution of the assets of the estate* is well illustrated by the closing sentence on page 38 of his brief and argument, where he says it is the duty of the receiver "to resist the diminishing of the estate by the payment to a general creditor in priority over all other creditors." We beg to ask how the creation of a preference or priority as between creditors can work a diminishing of the estate? And what possible interest has the receiver in the creation of such preference or priority?

The opinion of the Court of Appeals in this case announces no new or startling doctrine, though it defines clearly and concisely the relation of the receiver to creditors, and justly rebukes the conduct of the receiver in making himself the partisan champion of the interests of one creditor as against another. It is

the receiver who has attempted an innovation in practice, which the Court of Appeals saw fit to rebuke.

Appellee's claim matured four years ago, and on every principle of equity its payment should not longer be delayed—especially when payment has never been resisted by any party in interest. We respectfully ask that the receiver be permitted to thwart no longer the ends of justice, and that his petition for a writ of certiorari be denied.

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